

**CITY OF LITCHFIELD, MICHIGAN**  
**FINANCIAL STATEMENTS**  
**AND INDEPENDENT AUDITOR'S REPORT**  
**YEAR ENDED JUNE 30, 2004**

## AUDITING PROCEDURES REPORT

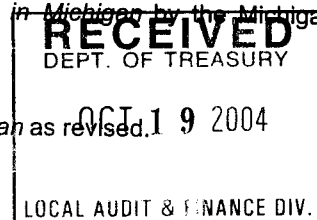
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Local Government Type <input checked="" type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Government Name CITY OF LITCHFIELD	County HILLSDALE
Audit Date 06/30/2004	Opinion Date 08/27/2004	Date Accountant Report Submitted to State:	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.



We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ yes ☒ no 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ yes ☒ no 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☒ yes ☐ no 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ yes ☒ no 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ yes ☒ no 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ yes ☒ no 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ yes ☒ no 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ yes ☒ no 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ yes ☒ no 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

### We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	X		
Reports on individual federal financial assistance programs (program audits).			X
Single Audit Reports (ASLGU).			X

Certified Public Accountant (Firm Name) OSBOURNE, MARCH, CONDON & CO., P.C.			
Street Address 184 W GARLETON ROAD	City HILLSDALE	State MI	ZIP 49242
Accountant Signature 			

CITY OF LITCHFIELD, MICHIGAN

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Osbourne, March, Condon & Co., P.C.

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## INDEPENDENT AUDITOR'S REPORT

To the City Council  
City of Litchfield, Michigan  
Litchfield, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Litchfield, Michigan, as of and for the year ended June 30, 2004, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of the Litchfield Fire Department, a joint venture between the City of Litchfield, Michigan and Litchfield Township, which the financial statements reflect the City's total share of assets and revenues constituting one percent of the related consolidated totals. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Litchfield Fire Department, a joint venture between the City of Litchfield, Michigan and Litchfield Township, is based solely on the report of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the report of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Litchfield, Michigan, as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated August 27, 2004 on our consideration of City of Litchfield, Michigan's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of the audit performed in accordance with *Government Auditing Standards*, and should be read in conjunction with this report in considering the results of our audit.

As described in NOTE 15, the City of Litchfield, Michigan has implemented a new financial reporting model, as required by the provisions of GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as of June 30, 2004.

The Management's Discussion and Analysis on pages III through VII is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the method of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

The accompanying required supplemental information, identified in the table of contents, is not required parts of the basic financial statements. The required supplemental information is information required by the Governmental Accounting Standards Board. Our audit was conducted for the purpose of forming opinions on the financial statements. The required supplemental information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Casbourne, March, Condon + Co., P.C.*

Certified Public Accountants

Hillsdale, Michigan  
August 27, 2004

Management's Discussion and Analysis

The following discussion and analysis of the financial performance for the City of Litchfield (the "City") provides an overview of the City's financial activities for the fiscal year ended June 30, 2004. Please read it in conjunction with the City's financial statements.

**Financial Highlights**

The following represents the most significant financial highlights for the year ended June 30, 2004:

- The financial report for the year ended June 30, 2004 reflects complete implementation of Governmental Accounting Standards Board Statement Number 34, which significantly changed the content and format of municipal financial reporting. Accordingly, these statements present both entity-wide financial reporting for all governmental and business activities in addition to reporting financial information at the fund level. A reconciliation of the net change in fund balance to the change in net assets is provided on page 28.
- Property taxes are the City's single, largest source of revenue. The City's tax base, net of captured taxable value, for fiscal year 2004 was \$24,262,544, which represents an increase of \$589,190 or 2.5 percent.
- State-shared revenue, the second largest revenue source, was reduced by the State of Michigan by approximately \$12,800 this year. This represents an 8 percent decrease from the prior year.
- Act 51 monies, received from gasoline tax through the State of Michigan, the third largest revenue source, increased by approximately \$17,200 this year. This represents a 14 percent increase from the prior year.

**Using the Annual Report**

This annual report consists of a series of financial statements. The statement of net assets and the statement of activities provide information about the activities of the City as a whole and present a longer-term view of the City's finances. This longer-term view uses the accrual basis of accounting so that it can measure the cost of providing services during the current year and whether the taxpayers have funded the full cost of providing government services.

The fund financial statements present a short-term view; they tell us how the taxpayers' resources were spent during the year, as well as how much is available for future spending. Fund financial statements also report the City's operations in more detail than the government-wide financial statements by providing information about activities for which the City acts solely as a trustee or agent for the benefit of those outside of the government.

# CITY OF LITCHFIELD, MICHIGAN

## Management's Discussion and Analysis

### The City as a Whole

The following table shows, in a condensed format, the net assets as of the current year ended June 30, 2004 compared to the prior year:

	Governmental Activities		Business-type Activities		Total	
	2004	2003	2004	2003	2004	2003
Current assets	\$ 499,233	\$ 541,639	\$ 1,267,800	\$ 1,118,966	\$ 1,767,033	\$ 1,660,605
Noncurrent assets	1,226,787	1,224,828	2,638,745	2,761,416	3,865,532	3,986,244
<b>Total Assets</b>	<b>\$ 1,726,020</b>	<b>\$ 1,766,467</b>	<b>\$ 3,906,545</b>	<b>\$ 3,880,382</b>	<b>\$ 5,632,565</b>	<b>\$ 5,646,849</b>
Current liabilities	\$ 56,057	\$ 75,221	\$ 151,395	\$ 122,687	\$ 207,452	\$ 197,908
Long-term liabilities	35,231	64,747	1,030,000	1,145,000	1,065,231	1,209,747
<b>Total Liabilities</b>	<b>\$ 91,288</b>	<b>\$ 139,968</b>	<b>\$ 1,181,395</b>	<b>\$ 1,267,687</b>	<b>\$ 1,272,683</b>	<b>\$ 1,407,655</b>
Net assets:						
Invested in capital -						
Net of related debt	\$ 1,156,973	\$ 1,135,304	\$ 1,493,746	\$ 1,240,845	\$ 2,650,719	\$ 2,376,149
Restricted	9,259	3,790	196,928	182,028	206,187	185,818
Unrestricted	468,500	487,405	1,034,476	1,189,822	1,502,976	1,677,227
<b>Total Net Assets</b>	<b>\$ 1,634,732</b>	<b>\$ 1,626,499</b>	<b>\$ 2,725,150</b>	<b>\$ 2,612,695</b>	<b>\$ 4,359,882</b>	<b>\$ 4,239,194</b>
<b>Total Net Assets and Liabilities</b>	<b>\$ 1,726,020</b>	<b>\$ 1,766,467</b>	<b>\$ 3,906,545</b>	<b>\$ 3,880,382</b>	<b>\$ 5,632,565</b>	<b>\$ 5,646,849</b>

The City's combined net assets increased by approximately 2.5 percent from a year ago – increasing from \$4.2 million to \$4.3 million.

The decrease in unrestricted net assets of governmental activities in the amount of \$19,000 is primarily due to the net decrease in compensated absences during the year.

Unrestricted net assets decreased by \$155,000 for business-type activities. This represents a decrease of approximately 13 percent. An unrestricted net asset is the part of net assets that can be used to finance day-to-day operations. A significant portion of that decrease was expected for two reasons. First, there was a \$23,000 capital acquisition for a new vehicle. Secondly, a contribution in the amount of \$150,000 received from the City's Tax Increment Financing Authority was used to pay down the principal on debt related to capital investments in the amount of \$110,000. The remaining \$15,000 (\$150,000 - \$110,000 principal - \$25,000 interest) was restricted for the retirement of debt.

# CITY OF LITCHFIELD, MICHIGAN

## Management's Discussion and Analysis

Prior year data is not available for the government-wide results of operations. Comparative analysis will be provided in future years when prior year information is available. The following is the government-wide results of operations for the fiscal year ended June 30, 2004:

	Governmental Activities 2004	Business- type Activities 2004
Revenue		
Program revenue:		
Charges for services	\$ 56,619	\$ 328,684
Operating grants and Contributions	142,523	165
General revenue:		
Property taxes	356,880	
State-shared revenues	143,234	
Licenses and permits	9,008	
Fines, fees, and forfeits	6,026	
Interest	11,477	15,426
Other	380	
TIFA contribution	63,000	150,000
Lease revenue	5,385	
Transfers	44,800	(44,800)
Total Revenue	\$ 839,332	\$ 449,475
Program Expenses		
General government	\$ 253,798	\$
Public safety	292,800	
Highways and streets	52,786	
Public works	80,854	
Parks and recreation	64,982	
Interest on long-term debt	3,513	
Depreciation (unallocated)	31,778	
Water		111,279
Sewer		192,947
Refuse		40,540
Total Program Expenses	\$ 780,511	\$ 344,766
Change in Net Assets	\$ 58,821	\$ 104,709

Management's Discussion and Analysis

**Governmental Activities**

In fiscal year 2004, decreases experienced in a few revenue categories are due to statewide economic conditions. The revenue categories impacted include State-shared revenue and investment earnings. Those losses of revenue were offset by an increase in the City's tax base and Act 51 monies, revenue received from the State of Michigan from gasoline tax for local and major street operations. The increase in property tax base is a result of inflationary increases in existing parcels. There has been no increase in the operating millage rate. The City millage rate continues at 13 mills.

As expected, expenses remained at a consistent level, with the exception of increases in personnel costs in various departments.

**Business-type Activities**

The City's business-type activities consist of the Water, Sewer and Refuse Funds. The City operates both Water and Sewer facilities. Refuse collection and recycling services are provided by an outside commercial entity.

Charges for services in the Water and Sewer operations decreased by 2.25% in light of increases in user rates, primarily due to, the decline in water consumption by the community. This is attributable to cooler summer weather conditions in recent years. Furthermore, expenses decreased by 1.9% due to a decline in maintenance and repair costs.

**The City's Funds**

The City's major funds are reported beginnings on page 11, following the government-wide financial statements. The fund financial statements provide detailed information about the significant funds, not the City as a whole. The City Council creates funds to help manage money for specific purposes as well as to show accountability for certain activities. The City's major funds for 2004 include the General Fund and Major Street Fund.

**General Fund Highlights**

The General Fund accounts for all police, fire, public works, planning and zoning, and administrative functions of the City government. The budget is essentially a "maintenance" budget, which means it increases modestly from year to year. The budget is monitored closely and amended periodically. The result is that actual revenues and expenses are usually within 5 percent of budgeted amounts.

The General Fund pays for most of the City's governmental services. The most significant are police and fire, which incurred expenses of approximately \$292,800 in 2004. Expenses for police and fire services are recorded in various departments within the General Fund.

**Capital Asset and Debt Administration**

At the end of fiscal year 2004, the City had approximately \$3,836,000 (net of depreciation) invested in a broad range of capital assets, including buildings, police and fire equipment, public works equipment, and water and sewer facilities. There is no related infrastructure reported in the year end net capital investment. The City elected to follow the method of prospective reporting of infrastructure assets provided in the new reporting pronouncement.

Management's Discussion and Analysis

**Capital Asset and Debt Administration (Concluded)**

The City continues to pay down debt obligations related to capital investments. Outstanding revenue bonds, for the construction of sewer facilities, reported in the Sewer Fund in the amount of \$1,145,000 represents 97% of the City's total debt obligations at June 30, 2004. Historically, the City's Tax Increment Financing Authority has contributed \$150,000 annually towards the repayment of the debt.

The City also funds equipment replacements by setting aside cash in the General Fund and maintains an Equipment Fund. The Equipment Fund charges City departments for the use of equipment. Monies collected accumulate towards the replacement of equipment. The City properly maintains existing equipment and carefully plans for equipment replacements to avoid burdening taxpayers with additional debt millage to replace existing equipment.

**Economic Factors and Next Year's Budgets and Rates**

The general operating millage will not be increased for next year, despite no projected increase in State-shared revenue. Certain expenditures are assumed to continue beyond the rate of inflation, such as health care insurance and liability insurance. Expenditures relating to contract agreements with Litchfield Township pertaining to (1) the Litchfield Fire Department, a joint venture between the City and Township and (2) personnel shared between the City and Township for cemetery purposes may vary from the current year if changes occur to said agreements in the subsequent period.

The City in response to the requirement of the new reporting model created two new funds, Refuse Fund and Internal Service Fund. The two funds activity was previously reported in the General Fund. This change negatively impacted the City's June 30, 2004 net change in fund balance by approximately \$47,000.

The Refuse Fund was created as a proprietary fund type since it meets the definition of an enterprise fund. Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the costs of providing goods or services to the general public on a continuing basis be financed or recovered through user charges.

The Internal Service Fund was created to account for shared machinery and equipment purchases and maintenance provided to other departments of the City on a cost reimbursement basis.

The effect of these two newly established funds on the General Fund 2004-2005 budget will be reviewed by City Council and appropriate adjustments will be made.

There were no significant variances between budget and actual results.

**Contacting the City's Management**

This financial report is intended to provide our citizens, taxpayers, customers, and investors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report, or need additional information, or would like to obtain financial statements of the City's component units, Tax Increment Finance Authority (TIFA) or Downtown Development Authority (DDA), we welcome you to contact the City's Administrative office located at 221 Jonesville Street, Litchfield, Michigan 49252.

CITY OF LITCHFIELD, MICHIGAN  
GOVERNMENT-WIDE FINANCIAL STATEMENTS  
STATEMENT OF NET ASSETS

JUNE 30, 2004

	PRIMARY GOVERNMENT		
	GOVERNMENTAL ACTIVITIES	BUSINESS ACTIVITIES	TOTAL
<b>ASSETS</b>			
Current Assets:			
Cash and cash equivalents	\$ 438,732	\$ 1,255,365	\$ 1,694,097
Accounts receivable	985	5,007	5,992
Note receivable - current portion	5,000		5,000
Due from other governments	9,253		9,253
Due from agency fund	19,598		19,598
Internal balances	25,665		25,665
Inventory		7,428	7,428
Total Current Assets	<u>\$ 499,233</u>	<u>\$ 1,267,800</u>	<u>\$ 1,767,033</u>
Noncurrent Assets			
Note receivable, net of current portion	\$ 12,500	\$	\$ 12,500
Investment in joint venture	17,146		17,146
Investment in land			
Capital assets	1,552,302	6,229,360	7,781,662
Furniture and equipment	(355,161)	(3,590,615)	(3,945,776)
Total Noncurrent Assets	<u>\$ 1,226,787</u>	<u>\$ 2,638,745</u>	<u>\$ 3,865,532</u>
<b>TOTAL ASSETS</b>	<u><u>\$ 1,726,020</u></u>	<u><u>\$ 3,906,545</u></u>	<u><u>\$ 5,632,565</u></u>
<b>LIABILITIES AND NET ASSETS</b>			
Current Liabilities:			
Accounts payable	\$ 9,252	\$ 5,005	\$ 14,257
Long-term debt, current portion	23,557	115,000	138,557
Compensated absences, current portion	6,000		6,000
Accrued liabilities	17,248		17,248
Accrued interest		5,725	5,725
Internal balances		25,665	25,665
Total Current Liabilities	<u>\$ 56,057</u>	<u>\$ 151,395</u>	<u>\$ 207,452</u>
Noncurrent Liabilities:			
Compensated absences, net of current portion	\$ 18,620	\$	\$ 18,620
Long-term debt, net of current portion	16,611	1,030,000	1,046,611
Total Noncurrent Liabilities	<u>\$ 35,231</u>	<u>\$ 1,030,000</u>	<u>\$ 1,065,231</u>
<b>TOTAL LIABILITIES</b>	<u><u>\$ 91,288</u></u>	<u><u>\$ 1,181,395</u></u>	<u><u>\$ 1,272,683</u></u>
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt	\$ 1,156,973	\$ 1,493,746	\$ 2,650,719
Restricted for bond repayment		196,928	196,928
Restricted for police training	918		918
Restricted for recreation activities	8,341		8,341
Unrestricted	468,500	1,034,476	1,502,976
TOTAL NET ASSETS	<u>\$ 1,634,732</u>	<u>\$ 2,725,150</u>	<u>\$ 4,359,882</u>
<b>TOTAL NET ASSETS AND LIABILITIES</b>	<u><u>\$ 1,726,020</u></u>	<u><u>\$ 3,906,545</u></u>	<u><u>\$ 5,632,565</u></u>

See accompanying notes to the basic financial statements.

COMPONENT UNITS	
TAX INCREMENT FINANCING AUTHORITY	DOWNTOWN DEVELOPMENT AUTHORITY
\$ 2,584,756	\$ 8,580
1,910	1,300
48,166	
<u>\$ 2,634,832</u>	<u>\$ 9,880</u>
\$	\$ 6,935
127,350	
350,000	
(37,800)	
<u>\$ 439,550</u>	<u>\$ 6,935</u>
<u>\$ 3,074,382</u>	<u>\$ 16,815</u>
\$	\$
	1,300
	800
<u>\$</u>	<u>\$ 2,100</u>
\$	\$
	8,700
<u>\$</u>	<u>\$ 8,700</u>
<u>\$</u>	<u>\$ 10,800</u>
\$ 312,200	\$
<u>2,762,182</u>	<u>6,015</u>
<u>\$ 3,074,382</u>	<u>\$ 6,015</u>
<u>\$ 3,074,382</u>	<u>\$ 16,815</u>

CITY OF LITCHFIELD, MICHIGAN  
GOVERNMENT-WIDE FINANCIAL STATEMENTS

STATEMENT OF ACTIVITIES

YEAR ENDED JUNE 30, 2004

		PROGRAM REVENUES	
	EXPENSES	CHARGES FOR SERVICES	OPERATING GRANTS AND CONTRIBUTIONS
GOVERNMENTAL ACTIVITIES			
PRIMARY GOVERNMENT			
Governmental Activities:			
General government	\$ 253,798	\$ 47,351	\$ 5,761
Public safety	292,800		
Highways and streets	52,786		122,710
Public works	80,854		
Parks and recreation	64,982	9,268	14,052
Interest on long-term debt	3,513		
Depreciation (unallocated)	31,778		
Total Governmental Activities	\$ 780,511	\$ 56,619	\$ 142,523
Business-type Activities:			
Sewer Fund	\$ 192,947	\$ 111,964	\$ -
Water Fund	111,279	170,041	165
Refuse Fund	40,540	46,679	
Total Business-type Activities	\$ 344,766	\$ 328,684	\$ 165
TOTAL PRIMARY GOVERNMENT	\$ 1,125,277	\$ 385,303	\$ 142,688
COMPONENT UNITS			
Tax Increment Finance	\$ 560,903	\$ -	\$ -
Downtown Development	4,352		
TOTAL COMPONENT UNITS	\$ 565,255	\$ -	\$ -

GENERAL REVENUES

Property taxes  
State-shared revenues  
Licenses and permits  
Fines, fees, and forfeits  
Interest  
Other  
Tifa contribution  
Gain on sale of property  
Lease revenue  
Transfers

TOTAL GENERAL REVENUES

CHANGE IN NET ASSETS

NET ASSETS - BEGINNING OF YEAR (RESTATED)

NET ASSETS - END OF YEAR

See accompanying notes to the basic financial statements.

NET (EXPENSE) REVENUE AND CHANGES IN NET ASSETS

PRIMARY GOVERNMENT			COMPONENT UNITS	
GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL	TAX INCREMENT FINANCING AUTHORITY	DOWNTOWN DEVELOPMENT AUTHORITY
\$ (200,686)	\$	\$ (200,686)	\$	\$
(292,800)		(292,800)		
69,924		69,924		
(80,854)		(80,854)		
(41,662)		(41,662)		
(3,513)		(3,513)		
(31,778)		(31,778)		
<u>\$ (581,369)</u>	<u>\$</u>	<u>\$ (581,369)</u>	<u>\$</u>	<u>\$</u>
\$	\$ (80,983)	\$ (80,983)	\$	\$
	58,927	58,927		
	6,139	6,139		
<u>\$</u>	<u>\$ (15,917)</u>	<u>\$ (15,917)</u>	<u>\$</u>	<u>\$</u>
<u>\$ (581,369)</u>	<u>\$ (15,917)</u>	<u>\$ (597,286)</u>	<u>\$</u>	<u>\$</u>
\$	\$	\$	\$ (560,903)	\$
				(4,352)
<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$ (560,903)</u>	<u>\$ (4,352)</u>
\$ 356,880	\$	\$ 356,880	\$ 742,239	\$ 2,354
143,234		143,234		
9,008		9,008		
6,026		6,026		
11,477	15,426	26,903	32,767	13
380		380		3,000
63,000	150,000	213,000		
5,385		5,385		3,875
44,800	(44,800)		16,500	
<u>\$ 640,190</u>	<u>\$ 120,626</u>	<u>\$ 760,816</u>	<u>\$ 791,506</u>	<u>\$ 9,242</u>
\$ 58,821	\$ 104,709	\$ 163,530	\$ 230,603	\$ 4,890
1,575,911	2,620,441	4,196,352	2,843,779	1,125
<u>\$ 1,634,732</u>	<u>\$ 2,725,150</u>	<u>\$ 4,359,882</u>	<u>\$ 3,074,382</u>	<u>\$ 6,015</u>

CITY OF LITCHFIELD, MICHIGAN  
BALANCE SHEET - GOVERNMENTAL FUNDS  
JUNE 30, 2004

	MAJOR FUNDS		OTHER NONMAJOR GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
	GENERAL	MAJOR STREET		
ASSETS				
Cash and cash equivalents	\$ 247,760	\$ 150,526	\$ 40,446	\$ 438,732
Accounts receivable	24			24
Due from other governmental units		6,980	2,273	9,253
Due from other funds	19,598			19,598
TOTAL ASSETS	<u>\$ 267,382</u>	<u>\$ 157,506</u>	<u>\$ 42,719</u>	<u>\$ 467,607</u>
LIABILITIES AND FUND BALANCES				
Liabilities				
Accounts payable	\$ 9,252	\$	\$	\$ 9,252
Accrued liabilities	14,748		2,500	17,248
Total Liabilities	<u>\$ 24,000</u>	<u>\$</u>	<u>\$ 2,500</u>	<u>\$ 26,500</u>
Fund Balances				
Reserved for:				
Police training - state funding	\$ 918	\$	\$	\$ 918
Recreation - donor restricted			8,341	8,341
Board Designated	35,011			35,011
Unreserved, undesignated	207,453	157,506	31,878	396,837
Total Fund Balances	<u>\$ 243,382</u>	<u>\$ 157,506</u>	<u>\$ 40,219</u>	<u>\$ 441,107</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 267,382</u>	<u>\$ 157,506</u>	<u>\$ 42,719</u>	<u>\$ 467,607</u>

See accompanying notes to the basic financial statements.

CITY OF LITCHFIELD, MICHIGAN  
RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET  
WITH THE STATEMENT OF NET ASSETS  
YEAR ENDED JUNE 30, 2004

GOVERNMENTAL FUND BALANCE \$ 441,107

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources, and  
are not reported in the funds.

The cost of the capital assets is	1,552,302	
Accumulated depreciation is	<u>(355,161)</u>	
		1,197,141

Receivables are expected to be collected in future years and are not available to pay for current  
year expenditures 18,461

Long-term liabilities are not due and payable in the current period and are not reported in the funds

Leases	(40,168)
Compensated absences	(24,620)

Internal Service Funds are also included as governmental activities to the extent of activity  
occurring between governmental funds and the Internal Service Fund 25,665

Investments in joint ventures are included as part of governmental activities 17,146

NET ASSETS OF GOVERNMENTAL ACTIVITIES \$ 1,634,732

See accompanying notes to the basic financial statements.

## CITY OF LITCHFIELD, MICHIGAN

## STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES -

## GOVERNMENTAL FUNDS

YEAR ENDED JUNE 30, 2004

	MAJOR FUNDS		NONMAJOR	TOTAL
	GENERAL	MAJOR STREET	GOVERNMENTAL FUNDS	GOVERNMENTAL FUNDS
REVENUES				
Taxes	\$ 356,880	\$	\$	\$ 356,880
Federal revenues	883			883
State revenues	148,112	95,091	27,619	270,822
Charges for services	47,351		8,087	55,438
Licenses and permits	9,008		1,181	10,189
Fines, fees, and forfeits	6,026			6,026
Charitable contributions			14,052	14,052
Component unit contributions	50,875			50,875
Interest	9,375	1,762	340	11,477
Lease revenue	5,385			5,385
Other	12,505			12,505
TOTAL REVENUES	\$ 646,400	\$ 96,853	\$ 51,279	\$ 794,532
EXPENDITURES				
Current:				
General government	\$ 292,824	\$	\$	\$ 292,824
Police	260,606			260,606
Highways and streets		41,701	18,918	60,619
Public works	86,760			86,760
Parks and recreation	27,357		45,457	72,814
Debt service:				
Principal	30,572			30,572
Interest	3,513			3,513
Capital outlay	24,421			24,421
TOTAL EXPENDITURES	\$ 726,053	\$ 41,701	\$ 64,375	\$ 832,129
REVENUES OVER (UNDER) EXPENDITURES	\$ (79,653)	\$ 55,152	\$ (13,096)	\$ (37,597)
OTHER FINANCING SOURCES (USES):				
Operating transfers in	\$ 54,000	\$	\$ 27,945	\$ 81,945
Operating transfers out	(37,945)	(6,000)	(3,200)	(47,145)
TOTAL OTHER FINANCING SOURCES (USES)	\$ 16,055	\$ (6,000)	\$ 24,745	\$ 34,800
REVENUES AND OTHER SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING (USES)	\$ (63,598)	\$ 49,152	\$ 11,649	\$ (2,797)
FUND BALANCES - BEGINNING OF YEAR (RESTATED)	306,980	108,354	28,570	443,904
FUND BALANCES - END OF YEAR	\$ 243,382	\$ 157,506	\$ 40,219	\$ 441,107

See accompanying notes to the basic financial statements.

CITY OF LITCHFIELD, MICHIGAN

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES  
IN FUND BALANCES OF GOVERNMENTAL FUNDS  
TO THE STATEMENT OF ACTIVITIES

YEAR ENDED JUNE 30, 2004

NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS \$ (2,797)

Amounts reported for governmental activities in the statement of activities are different because:

Governmental funds report capital outlays as expenditures, and in the statement of activities these costs are allocated over their estimated useful lives as depreciation:

Depreciation expense	\$ (31,778)	
Capital outlay	<u>22,875</u>	(8,903)

Net income from joint venture is not recorded in the governmental funds, but is recorded in the statement of activities. 4,080

Repayment of capital leases is an expenditure in the governmental funds, but not in the statement of activities (where it reduces long-term debt). 30,572

In the statement of activities, compensated absences (sick leave and vacations) are measured by the amounts earned during the year. Therefore, when leave time is earned it is recognized as expenditures in the statement of activities. In the governmental funds, however, expenditures for these items are measured by the amount of financial resources used (essentially, the amounts actually paid). This year, vacation and sick leave used (or actually paid) exceeded the amounts earned. 15,387

Internal Service Funds are also included as governmental activities to the extent of activity occurring between governmental funds and the Internal Service Fund. 25,665

Included in governmental activities is an expenditure for the forgiveness of the current amount due from a local industrial corporation on a long-term note receivable. Where as, governmental funds recognize revenue and expenditures when cash is either collected or disbursed. (5,183)

CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES \$ 58,821

See accompanying notes to the basic financial statements.

## CITY OF LITCHFIELD, MICHIGAN

## PROPRIETARY FUNDS

## STATEMENT OF NET ASSETS

JUNE 30, 2004

	ENTERPRISE FUNDS	
	MAJOR FUND	
	SEWER	WATER
<b>ASSETS</b>		
Current Assets:		
Cash	\$ 901,489	\$ 305,089
Accounts receivables	2,059	2,506
Due from other funds	25,000	
Inventory		7,428
Total Current Assets	<u>\$ 928,548</u>	<u>\$ 315,023</u>
Noncurrent Assets:		
Capital assets	\$ 4,216,987	\$ 1,786,640
Accumulated depreciation	(2,648,853)	(831,707)
Total Noncurrent Assets	<u>\$ 1,568,134</u>	<u>\$ 954,933</u>
<b>TOTAL ASSETS</b>	<u><u>\$ 2,496,682</u></u>	<u><u>\$ 1,269,956</u></u>
<b>LIABILITIES AND NET ASSETS</b>		
Current Liabilities		
Accounts payable	\$ 1,302	\$ 3,703
Long-term debt, current portion	115,000	
Accrued liabilities		
Accrued Interest	5,725	
Due to other funds		25,000
Total Current Liabilities	<u>\$ 122,027</u>	<u>\$ 28,703</u>
Noncurrent Liabilities		
Long-term debt, net of current portion	<u>\$ 1,030,000</u>	<u>\$</u>
Total Liabilities	<u>\$ 1,152,027</u>	<u>\$ 28,703</u>
Net Assets		
Invested in capital assets, net of related debt	\$ 417,409	\$ 954,933
Restricted	196,928	
Unrestricted	730,318	286,320
Total Net Assets	<u>\$ 1,344,655</u>	<u>\$ 1,241,253</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u><u>\$ 2,496,682</u></u>	<u><u>\$ 1,269,956</u></u>

See accompanying notes to the basic financial statements.

ENTERPRISE FUNDS		INTERNAL SERVICE FUND
NONMAJOR FUND		
REFUSE	TOTAL	EQUIPMENT
\$ 5,697	\$ 1,212,275	\$ 43,090
442	5,007	
	25,000	
	7,428	
\$ 6,139	\$ 1,249,710	\$ 43,090
\$	\$ 6,003,627	\$ 225,733
	(3,480,560)	(110,055)
\$	\$ 2,523,067	\$ 115,678
\$ 6,139	\$ 3,772,777	\$ 158,768
\$	\$ 5,005	\$
	115,000	
	-	
	5,725	
	25,000	
\$	\$ 150,730	\$
\$	\$ 1,030,000	\$
\$	\$ 1,180,730	\$
\$	\$ 1,372,342	\$ 115,678
	196,928	
6,139	1,022,777	43,090
\$ 6,139	\$ 2,592,047	\$ 158,768
\$ 6,139	\$ 3,772,777	\$ 158,768

CITY OF LITCHFIELD, MICHIGAN  
RECONCILIATION OF ENTERPRISE FUNDS BALANCE SHEET  
WITH THE STATEMENT OF NET ASSETS  
YEAR ENDED JUNE 30, 2004

ENTERPRISE FUND NET ASSETS	\$ 2,592,047
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Amounts reported for business activities in the statement of net assets are different because:

Internal Service Funds are also included as business activities to the extent of activity occurring between Enterprise Funds and the Internal Service Fund

Assets:		
Cash		43,090
The cost of the capital assets is	225,733	
Accumulated depreciation is	<u>(110,055)</u>	
		115,678
Liabilities:		
Due to governmental activities		(25,665)

NET ASSETS OF BUSINESS-TYPE ACTIVITIES	<u>\$ 2,725,150</u>
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See accompanying notes to the basic financial statements.

## CITY OF LITCHFIELD, MICHIGAN

## PROPRIETARY FUNDS

## STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

YEAR ENDED JUNE 30, 2004

	ENTERPRISE FUNDS	
	MAJOR FUNDS	
	SEWER	WATER
OPERATING REVENUES		
Charges for services	\$ 111,964	\$ 170,041
OPERATING EXPENSES		
General operations and maintenance	\$ 62,587	\$ 74,893
Depreciation	115,189	52,070
TOTAL OPERATING EXPENSES	\$ 177,776	\$ 126,963
OPERATING INCOME (LOSS)	\$ (65,812)	\$ 43,078
NON-OPERATING REVENUES (EXPENSES)		
Interest income	\$ 12,118	\$ 3,308
Interest expense	(30,855)	
Contributions	150,000	
Gain on sale of property		165
Wellhead protection grant		
TOTAL NET NON-OPERATING REVENUES	\$ 131,263	\$ 3,473
INCOME BEFORE OPERATING TRANSFERS	\$ 65,451	\$ 46,551
OPERATING TRANSFERS		
Operating transfers in	\$ (25,000)	\$ 200
Operating transfers out		(20,000)
TOTAL NET OPERATING TRANSFERS	\$ (25,000)	\$ (19,800)
NET INCOME	\$ 40,451	\$ 26,751
TOTAL NET ASSETS - BEGINNING OF YEAR	1,304,204	1,214,502
TOTAL NET ASSETS - END OF YEAR	\$ 1,344,655	\$ 1,241,253

See accompanying notes to the basic financial statements.

<u>ENTERPRISE FUNDS</u>		<u>INTERNAL SERVICE FUND</u>
<u>NON- MAJOR FUND</u>		
<u>REFUSE</u>	<u>TOTAL</u>	<u>EQUIPMENT</u>
<u>\$ 46,679</u>	<u>\$ 328,684</u>	<u>\$ 39,359</u>
<u>\$ 40,540</u>	<u>\$ 178,020</u>	<u>\$ 11,709</u>
	<u>167,259</u>	<u>11,118</u>
<u>\$ 40,540</u>	<u>\$ 345,279</u>	<u>\$ 22,827</u>
<u>\$ 6,139</u>	<u>\$ (16,595)</u>	<u>\$ 16,532</u>
<u>\$</u>	<u>\$ 15,426</u>	<u>\$</u>
	<u>(30,855)</u>	
	<u>150,000</u>	<u>30,000</u>
	<u>165</u>	<u>501</u>
<u>\$</u>	<u>\$ 134,736</u>	<u>\$ 30,501</u>
<u>\$ 6,139</u>	<u>\$ 118,141</u>	<u>\$ 47,033</u>
<u>\$</u>	<u>\$ 200</u>	<u>\$ 10,000</u>
	<u>(45,000)</u>	
<u>\$</u>	<u>\$ (44,800)</u>	<u>\$ 10,000</u>
<u>\$ 6,139</u>	<u>\$ 73,341</u>	<u>\$ 57,033</u>
	<u>2,518,706</u>	<u>101,735</u>
<u>\$ 6,139</u>	<u>\$ 2,592,047</u>	<u>\$ 158,768</u>

CITY OF LITCHFIELD, MICHIGAN

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENSES, AND CHANGES  
IN NET ASSETS TO THE STATEMENT OF ACTIVITIES

YEAR ENDED JUNE 30, 2004

NET CHANGE IN NET ASSETS - TOTAL ENTERPRISE FUNDS \$ 73,341

Amounts reported for business activities in the statement of activities are different because:

Internal Service Funds are also included as business activities to the extent of activity  
occurring between Enterprise Funds and the Internal Service Fund 31,368

CHANGE IN NET ASSETS OF BUSINESS ACTIVITIES \$ 104,709

See accompanying notes to the basic financial statements.

## CITY OF LITCHFIELD, MICHIGAN

## PROPRIETARY FUNDS

## STATEMENT OF CASH FLOWS

YEAR ENDED JUNE 30, 2004

	ENTERPRISE FUNDS	
	MAJOR FUND	
	SEWER	WATER
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash receipts from customers	\$ 111,099	\$ 168,657
Cash receipts for interfund services provided		
Payments to employees	(22,527)	(27,212)
Payments to suppliers	(28,948)	(52,708)
Payments to interfund services provided	(10,336)	(10,859)
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ 49,288	\$ 77,878
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Wellhead Protection Grant proceeds	\$ 150,000	\$ 165
Contribution from component unit	(25,000)	(19,800)
Transfer to other funds		
NET CASH PROVIDED (USED) BY NONCAPITAL FINANCING ACTIVITIES	\$ 125,000	\$ (19,635)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Interest paid on capital debt	\$ (25,130)	\$
Principal paid on capital debt	(110,000)	
Interfund loan (payment) receipt	25,000	(25,000)
Proceeds from sale of equipment		
Purchase of capital assets	(11,450)	(11,450)
NET CASH (USED) BY CAPITAL AND RELATED FINANCING ACTIVITIES	\$ (121,580)	\$ (36,450)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest	\$ 12,118	\$ 3,308
NET CHANGE IN CASH	\$ 64,826	\$ 25,101
CASH - BEGINNING OF YEAR	836,663	279,988
CASH - END OF YEAR	\$ 901,489	\$ 305,089
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Operating income (loss)	\$ (65,812)	\$ 43,078
Adjustments to reconcile operating income to net cash provided (used) by operating activities:		
Depreciation expense	\$ 115,189	\$ 52,070
(Increase) decrease in:		
Accounts receivable	(866)	(1,384)
Inventories		(7,428)
Increase (decrease) in:		
Accounts payable	777	(8,458)
Total Adjustments	\$ 115,100	\$ 34,800
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ 49,288	\$ 77,878

See accompanying notes to the basic financial statements.

ENTERPRISE FUNDS		INTERNAL SERVICE FUND
NONMAJOR FUND		
REFUSE	TOTAL	EQUIPMENT
\$ 46,236	\$ 325,992	\$
	-	39,359
(40,539)	(49,739)	
	(122,195)	(11,709)
	(21,195)	
\$ 5,697	\$ 132,863	\$ 27,650
\$	\$ 165	\$
	150,000	40,000
	(44,800)	
\$	\$ 105,365	\$ 40,000
\$	\$ (25,130)	\$
	(110,000)	
	-	
	(22,900)	501
\$	\$ (158,030)	(32,807)
\$	\$ 15,426	\$
\$ 5,697	\$ 95,624	\$ 35,344
	1,116,651	7,746
\$ 5,697	\$ 1,212,275	\$ 43,090
\$ 6,139	\$ (16,595)	\$ 16,532
	\$ 167,259	\$ 11,118
(442)	(2,692)	
	(7,428)	
	-	
	(7,681)	
\$ (442)	\$ 149,458	\$ 11,118
\$ 5,697	\$ 132,863	\$ 27,650

CITY OF LITCHFIELD, MICHIGAN  
FIDUCIARY FUNDS  
STATEMENT OF ASSETS AND LIABILITIES  
JUNE 30, 2004

	AGENCY FUND	TRUST FUND
	TAX COLLECTION FUND	DEFERRED COMPENSATION
ASSETS		
Cash	\$ 67,764	\$
Investments with agents		287,171
	<u>\$ 67,764</u>	<u>\$ 287,171</u>
LIABILITIES		
Due to employees for deferred compensation	\$ 19,598	\$ 287,171
Due to other funds	48,166	
Due to other governmental units		
TOTAL LIABILITIES	<u>\$ 67,764</u>	<u>\$ 287,171</u>

See accompanying notes to the basic financial statements.

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2004

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the City of Litchfield, Michigan conform to generally accepted accounting principles as applicable to governments. The following is a summary of the more significant policies:

FINANCIAL REPORTING ENTITY

On June 1, 1970, the City of Litchfield, Michigan (the "City") adopted the Home Rule Charter. The City operates under a Council-Manager form of government and provides the following services as authorized by its charter: Public Safety (Police and Fire), Highways and Streets, Sanitation, Health, Recreation, Public Improvements, Planning and Zoning, and General Administrative Services.

As required by generally accepted accounting principles, the financial statements of the reporting entity include those of the City (the primary government) and its component units. The component units discussed below are included in the City's reporting entity because of the significance of its operational or financial relationship with the City.

In conformity with generally accepted accounting principles, the financial statements of the component units have been included in the financial reporting entity as discretely presented component units.

Discretely Presented Component Units - The component units columns in the combined financial statements include the financial data of the City's component units. The units are reported in a separate column to emphasize they are legally separate from the City.

Tax Increment Finance Authority (TIFA) - The Authority is governed by a separate board appointed by the City Council to promote economic growth in the TIFA district.

Downtown Development Authority - The Authority is governed by a separate board appointed by the City Council to formulate plans for design, promotion and organization, and economic restructuring of the City's downtown area.

Brownsfield Redevelopment Authority (BRA) - The Authority was established by the City during the year ended June 30, 2000, under the authority contained in Act 381, of the Michigan Public Acts of 1996, as amended. The Authority is governed by a separate board appointed by the City Council to facilitate the implementation of plans relating to the identification and treatment of environmentally distressed areas so as to promote revitalization in the City of Litchfield.

The combined financial statements do not include financial data of the Brownsfield Redevelopment Authority since it did not have any financial transactions during the year ended June 30, 2004.

Copies of the TIFA and DDA financial statements may be obtained at the City offices located at 221 Jonesville Street, Litchfield, Michigan 48167.

Joint Venture - Discussed at NOTE 2.

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

FINANCIAL REPORTING ENTITY (CONCLUDED)

In June 1999, the Governmental Accounting Standards Board (GASB) unanimously approved Statement No. 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*. Certain of the significant changes in the Statement include the following:

- For the first time the Authority's financial statements include:
  - A Management Discussion and Analysis (MD&A) section providing an analysis of the City's overall financial position and results of operations.
  - Financial statements prepared using full accrual accounting for all of the City's activities, including fixed assets (building, equipment, vehicles, etc.)
- A change in the fund financial statements to focus on major funds

ECONOMIC DEPENDENCY

The City is economically dependent on the State of Michigan for state shared revenues. Absent allocations from the State, the City's operating results would report expenditures exceeding revenues in its General, Major Street, and Local Street Funds. Furthermore, the aforementioned funds would be in a deficit position within a two year period continuing the programs the City currently offers.

GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the non-fiduciary activities of the City. For the most part the effect of inter-fund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. All the City's government wide activities are considered governmental activities.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenue includes (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Taxes, intergovernmental payments, and other items not included among program revenues are reported instead as general revenue.

Separate financial statements are provided for governmental funds and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds are reported as separate columns in the fund financial statements.

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS (CONTINUED)

Government-Wide Statements

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. The effect of inter-fund activity has been eliminated from the government-wide financial statements.

Fund Based Statements

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, expenditures related to compensated absences, and claims and judgments are recorded only when payment is due.

Revenues are recognized in the accounting period in which they become both measurable and available to finance expenditures of the fiscal period. Major revenue types for which receivables are recorded on the current accounting period's balance sheet include property taxes and State-shared revenues. All other revenue items are considered to be available only when cash is received by the City.

The City reports the following major governmental funds:

The *General Fund* is the general operating fund of the City. It is used to account for all financial resources of the general government, except those required to be accounted for in another fund.

The *Major Street Fund* is a Special Revenue Fund that accounts for revenue received from gasoline tax through the State of Michigan under Act 51. Expenditures of this fund include the maintenance of major streets, as well as improvement of roadways and related financing expenditures.

The City reports the following major proprietary funds:

The *Water and Sewer Funds* are the City's only major proprietary funds. They account for the activities of the water distribution and sewage collection systems.

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS (CONCLUDED)

Additionally, the City reports the following fund types:

Governmental Funds

*Special Revenue Funds* are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for certain purposes.

Proprietary Funds

*Enterprise Funds* are used to account for business-like activities provided to the general public. These activities are financed primarily by user charges and the measurement of financial activity focuses on net income measurement similar to the private sector.

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services in connection with a proprietary fund's principal ongoing operations. The principal operating revenue of the proprietary funds relates to charges to customers for services. Operating expenses for proprietary funds include the cost of services, administrative expenses, and depreciation of capital assets. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

The *Internal Service Fund* accounts for shared machinery and equipment purchases and maintenance provided to other departments of the City on a cost reimbursement basis. This fund accounted for 55% and 45% of its activity with business-type and governmental activities, respectively. As a result, the assets and equity were reported in business-type activities and the net profit was allocated on a pro rata basis based on the aforementioned activity percentages.

Fiduciary Funds (Not included in government-wide statements)

*Fiduciary Funds* are used to account for assets held in a trustee or agency capacity for others and therefore are not available to support City operations. Agency Funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. Agency funds are not included in the government-wide statements. The City presently collects and distributes property taxes on behalf of and to other local units of government.

Private-sector standards of accounting issued prior to December 1, 1989, are generally followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with the standards of the Governmental Accounting Standards Board.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this rule are charges between the City's water and sewer function and various other functions of the City. Elimination of these charges would distort costs and program revenues reported for the various functions concerned.

Amounts reported as program revenue include: (1) charges to customers or applicants for goods, services, or privileges provided; (2) operating grants and contributions. When expenses are incurred for purposes for which both restricted and unrestricted net assets are available, restricted net assets are used prior to unrestricted net assets.

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

BANK DEPOSITS

Cash includes cash on hand, demand deposits, savings, certificate of deposits and municipal mutual funds that are highly liquid.

RECEIVABLES AND PAYABLES

Outstanding balances between funds are reported as "due to/from other funds." Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year is referred to as "advances to/from other funds." Any residual balances outstanding between the governmental activities and the business-type activities are reported in the government-wide financial statements as "internal balances."

All trade and property tax receivables are reported at their net realizable values.

CAPITAL ASSETS

Capital assets that include land, buildings, improvements, equipment and vehicles are reported in the government wide financial statements. The City defines capital assets as assets with an initial individual cost of more than \$5,000 and an estimated useful life in excess of 1 year. Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. Costs of normal repair and maintenance that do not add to the value or materially extend assets life are not capitalized but rather expensed in the period incurred.

The City has elected under Governmental Accounting Standards Board Statement No. 34 not to report infrastructure retrospectively. Newly acquired or constructed infrastructure will be capitalized and depreciated over their useful lives. There were no additions to infrastructure during the year.

Buildings, improvements, equipment and vehicles are depreciated using the straight-line method over the following estimated useful lives:

	YEARS
Buildings	40
Improvements	20
Equipment	3-20
Vehicles	3

COMPENSATED ABSENCES

It is the City's policy to permit employees to accumulate earned but unused sick and vacation leave time. A total of 5 to 20 days vacation and 12 days of sick leave per year may be accumulated by each employee. Employees are allowed to accumulate and carryover ten vacation days to the following year with management approval. Otherwise vacation time not used is forfeited.

CITY OF LITCHFIELD, MICHIGAN

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2004

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

COMPENSATED ABSENCES (CONCLUDED)

Furthermore, employees are allowed to accumulate no more than sixty days of sick leave time. Upon termination of employment, if an employee has five consecutive years or more of employment service the employee will be paid one-fourth of their accumulated unused sick leave time. Employees with ten consecutive years or more of employment service will be paid one-half of their accumulated unused sick leave time upon termination.

Upon retirement, an employee will receive pay at their regular rate of pay for a maximum thirty days of accumulated unused sick leave time.

During the year the net decrease in compensated absences was \$15,386 leaving an ending balance of \$24,620.

LONG-TERM OBLIGATIONS

In the government-wide financial statements and the proprietary fund types reported in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund-type statement of net assets. If applicable, bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt. In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Issuance costs are reported as debt service expenditures.

FUND EQUITY

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONCLUDED)

PROPERTY TAX

The City of Litchfield, Michigan bills and collects property taxes and distributes them to other local units of government. Properties are assessed as of December 31, and the related real property taxes are levied and become a lien on July 1 of the following year for summer taxes and December 31 for winter taxes. Summer and winter taxes are due without penalty if paid by September 14 and February 28, respectively. Delinquent taxes are turned over to the County and added to the County tax roll. The County remits all uncollected delinquent real property tax to the City by June 30. Uncollected personal property taxes are not accrued because the date of collection is uncertain.

BUDGETS AND BUDGETARY ACCOUNTING

The City's procedures in establishing the budgetary data reflected in the financial statements are as follows:

1. The City Manager submits to the City Council a proposed operating budget for the fiscal year. The operating budget includes proposed expenditures and the means of financing them.
2. Public hearings are conducted to obtain taxpayer comments.
3. Prior to July 1, the budget is legally enacted through passage of an ordinance.
4. The City Manager is authorized to transfer budgeted amounts between departments within any fund; however, any revisions that change the total expenditures of any fund must be approved by the City Council.
5. Formal budgetary integration is employed as a management control device during the year for the General Fund and Special Revenue Funds.
6. Budgets for the General and Special Revenue Funds are adopted on a basis consistent with generally accepted accounting principles, which is the modified accrual basis used to reflect actual results, and consist only of those amounts contained in the formal budget approved or as amended by the City Council. The General Fund budget is adopted at the department level and all other funds are adopted at the fund level.

ENCUMBRANCE ACCOUNTING

Encumbrances for goods and services are documented by requisitions or contracts. Appropriations lapse at June 30 and any encumbrances outstanding at that time are to be either canceled or appropriately provided for in the subsequent year's budget. There were no outstanding encumbrances at June 30, 2004.

CITY OF LITCHFIELD, MICHIGAN

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2004

NOTE 2: JOINT VENTURE

The City participates with the Litchfield Township in the Litchfield Fire Department (the "Department"), a joint venture pursuant to an agreement entered into between the two parties. In accordance to the provisions of Governmental Accounting Standards Board No. 14 the joint venture results from the on going financial responsibility of the Department's operations agreed to by the aforementioned municipalities pursuant to the contractual agreement. A seven member Board of Directors comprised of two members of the City of Litchfield Council, two members of Litchfield Township Board, one member of Scipio Township and Butler Township Boards, and one member from the community at large govern the Department.

Either the City or Litchfield Township has the power to terminate the joint venture. However, notice of termination must be given six months prior to the Department's fiscal year end. Upon termination, all property of the Litchfield Fire Department will be liquidated and any outstanding indebtedness will be paid. The proceeds then remaining will be divided equally between the City of Litchfield, Michigan and the Litchfield Township.

The Department is funded by fire contracts with local townships and equal contributions made by the City of Litchfield, Michigan and the Litchfield Township. The Fire Department reported revenues in excess of expenditures in the amount of \$8,160 on its June 30, 2004 financial statements. The City of Litchfield, Michigan reported \$4,080 (fifty-percent) of the revenues over expenditures in its government-wide financial statements in governmental activities. The City's investment in the joint venture is reported in the statement of net assets under governmental activities in the amount of \$17,146.

At year end June 30, 2004 the Department does not have title to any real property or rescue vehicles. The City of Litchfield, Michigan and the Litchfield Township have title, either jointly or individually, to all fire rescue vehicles used in the Department's operations. Additionally, the City and the Township are mutually obligated in a capital lease agreement to finance a rescue vehicle; see NOTE 7.

Copies of the Fire Department's financial statements may be obtained at the City of Litchfield, Michigan offices.

NOTE 3: CASH AND INVESTMENTS

Michigan Compiled Laws, Section 129.91, authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The local unit is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States, repurchase agreements, bankers' acceptances of United States banks, commercial paper rated within the two highest classifications, which matures not more than 270 days after the date of purchase and not more than fifty percent of any fund may be invested, obligations of the State of Michigan or its political subdivisions, which are rated as investment grade, and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

The City has designated fifteen banks for the deposit of City funds. The investment policy adopted by the City Council in accordance with Public Act 196 of 1997 is in accordance with statutory authority.

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 3: CASH AND INVESTMENTS (CONCLUDED)

At year end, the deposits were reported in the basic financial statements in the following categories:

	Governmental Activities	Business-type Activities	Fiduciary Funds	Total Primary Government	Component Units
Cash	\$ 430,391	\$1,058,437	\$ 67,764	\$ 1,556,592	\$2,593,336
Cash – restricted	8,341	196,928		205,269	
	<u>\$ 438,732</u>	<u>\$1,255,365</u>	<u>\$ 67,764</u>	<u>\$ 1,761,861</u>	<u>\$2,593,336</u>
Investments	\$	\$	\$ 287,171	\$ 287,171	\$
Total	<u>\$ 438,732</u>	<u>\$1,255,365</u>	<u>\$ 354,935</u>	<u>\$ 2,049,032</u>	<u>\$2,593,336</u>

The breakdown between cash and investments for the City and component units are as follows:

	PRIMARY GOVERNMENT	COMPONENT UNITS
Cash (checking accounts, savings accounts and Certificates of Deposits)	\$ 1,761,143	\$ 2,593,336
Municipal mutual funds	618	
Petty cash	100	
Total	<u>\$ 1,761,861</u>	<u>\$ 2,593,336</u>

The bank balance of the City's deposits is \$4,285,533, of which \$2,136,727 is covered by federal depository insurance.

The investments of the City are categorized as follows to give an indication of the level of risk assumed by the City at year end:

- Category 1 Investments that are insured or registered or for which the securities are held by the City or its agent in the City's name.
- Category 2 Uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the City's name.
- Category 3 Uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent, but not in the City's name.

The City's investments at June 30, 2004 are summarized as follows:

INVESTMENTS	BOOK VALUE	MARKET VALUE	RISK CATEGORY
Employee Deferred Compensation Mutual Funds	<u>\$287,171</u>	<u>\$287,171</u>	Unclassified

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 4: CAPITAL ASSETS

Capital asset activity of the primary government was as follows:

	Balance <u>July 1, 2003</u>	<u>Additions</u>	<u>Disposals</u>	Balance <u>June 30, 2004</u>
<u>GOVERNMENTAL ACTIVITIES</u>				
Capital assets not being depreciated:				
Land	\$ 866,073	\$	\$	\$ 866,073
Capital assets being depreciated:				
Buildings and improvements	\$ 316,082	\$	\$	\$ 316,082
Equipment	266,192	22,875		289,067
Vehicles	63,080			63,080
Technology	18,000			18,000
Subtotal	<u>\$ 1,529,427</u>	<u>\$ 22,875</u>	<u>\$</u>	<u>\$ 1,552,302</u>
Accumulated depreciation:				
Buildings and improvements	\$ 178,269	\$ 5,298	\$	\$ 183,567
Equipment	103,034	14,946		117,980
Vehicles	40,080	7,667		47,747
Technology	2,000	3,867		5,867
Subtotal	<u>\$ 323,383</u>	<u>\$ 31,778</u>	<u>\$</u>	<u>\$ 355,161</u>
Net Capital Assets	<u><u>\$ 1,206,044</u></u>	<u><u>\$ (8,903)</u></u>	<u><u>\$</u></u>	<u><u>\$ 1,197,141</u></u>
<u>BUSINESS-TYPE ACTIVITIES</u>				
Capital assets not being depreciated:				
Land	\$ 265,571	\$	\$	\$ 265,571
Capital assets being depreciated:				
Water and sewer distribution system	\$ 5,715,156	\$	\$	\$ 5,715,156
Equipment	205,426	32,807	12,500	225,733
Vehicles		22,900		22,900
Subtotal	<u>\$ 6,186,153</u>	<u>\$ 55,707</u>	<u>\$ 12,500</u>	<u>\$ 6,229,360</u>
Accumulated depreciation:				
Water and sewer distribution system	\$ 3,313,301	\$ 164,587	\$	\$ 3,477,888
Equipment	111,437	11,118	12,500	110,055
Vehicles		2,672		2,672
Subtotal	<u>\$ 3,424,738</u>	<u>\$ 178,377</u>	<u>\$ 12,500</u>	<u>\$ 3,590,615</u>
Net Capital Assets	<u><u>\$ 2,761,415</u></u>	<u><u>\$ (122,670)</u></u>	<u><u>\$</u></u>	<u><u>\$ 2,638,745</u></u>

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 4: CAPITAL ASSETS (CONCLUDED)

Depreciation expense was charged to programs of the primary government as follows:

Governmental activities	<u>\$ 31,778</u>
Business-type activities	<u>\$178,377</u>

NOTE 5: NOTE RECEIVABLE

In January 1997 the City entered into an agreement to sell land to a local industrial company in the amount of \$50,000. The terms of the agreement require the local company to pay \$5,000 annually, including interest at 10%. However, if the local company achieves employment levels annually as stated in the agreement the City will forgive the annual payments, including interest, each year employment levels are met.

During the year the City forgave principal payments of \$5,000. At June 30, 2004 the outstanding balance due from the local company was \$17,500.

Future principal maturities to be collected from the local company are as follows:

<u>JUNE 30</u>	<u>AMOUNT</u>
2005	\$ 5,000
2006	5,000
2007	5,000
2008	<u>2,500</u>
	<u>\$17,500</u>

NOTE 6: OPERATING LEASE

During the year the City entered into a lease agreement to lease City owned farmland to a local individual. The terms of the lease require the local individual to pay the City \$5,385 annually, through May 31, 2005.

Future minimum lease payments to be received from the local individual are as follows:

<u>JUNE 30</u>	<u>AMOUNT</u>
2005	<u>\$ 5,385</u>

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 7: LONG-TERM DEBT

Long-term debt at June 30, 2004 is comprised of the following:

Capital lease payable to Emergency One for fire equipment, payable in annual installments of \$26,000 to \$33,000 at an annual interest rate of 5.64% through February 3, 2006	\$ 32,305
Capital lease payable to General Motors Acceptance Corporation for a police vehicle, payable in annual installments of \$7,900 to \$8,300 at an annual interest rate of 4.95% through July 1, 2005	7,863
Revenue Bonds, \$2,190,000 Michigan State Revolving Loan due in annual installments of \$25,000 to \$135,000 at an annual interest rate of 2% through April 1, 2014	<u>\$1,145,000</u>
	\$1,185,168
Less: current portion of long-term debt	<u>138,557</u>
<b>TOTAL LONG-TERM DEBT</b>	<u><b>\$1,046,611</b></u>

The following is a summary of changes in long-term debt:

	Balance July 1, 2003	Additions	Reductions	Balance June 30, 2004
<b>GOVERNMENTAL ACTIVITIES</b>				
Capital lease - General Motors Corp	\$ 23,607		\$ 15,744	\$ 7,863
Capital lease - Emergency One	47,133		14,828	32,305
Total Governmental Activities	<u>\$ 70,740</u>	<u>\$</u>	<u>\$ 30,572</u>	<u>\$ 40,168</u>
<b>BUSINESS-TYPE ACTIVITIES</b>				
Revenue bonds	<u>\$1,255,000</u>	<u>\$</u>	<u>\$ 110,000</u>	<u>\$1,145,000</u>
	<u><u>\$1,255,000</u></u>	<u><u>\$</u></u>	<u><u>\$ 140,572</u></u>	<u><u>\$1,185,168</u></u>

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 7: LONG-TERM DEBT (CONCLUDED)

The following is a schedule of principal and interest maturities:

	Governmental Activities			Business-type Activities		
	Principal	Interest	Total	Principal	Interest	Total
2005	\$ 23,557	\$ 3,000	\$ 26,557	\$ 115,000	\$ 22,900	\$ 137,900
2006	16,611	2,500	19,111	115,000	20,600	135,600
2007				120,000	18,300	138,300
2008				120,000	15,900	135,900
2009				125,000	13,500	138,500
2010-2014				550,000	29,300	579,300
	<u>\$ 40,168</u>	<u>\$ 5,500</u>	<u>\$ 45,668</u>	<u>\$1,145,000</u>	<u>\$ 120,500</u>	<u>\$1,265,500</u>

NOTE 8: DEFERRED COMPENSATION PLAN

The City offers eligible employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The Plan, available to all full-time employees, permits them to defer a portion of their salary until future years. The City matches employee contributions into the Plan up to a maximum of 7.0% of the employees' base pay, excluding overtime. Employees are 100% vested in employer contributions, and earnings there on. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency.

All amounts of compensation deferred under the Plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are (until paid or made available to the employee or other beneficiary) solely the property and rights of the City, (without being restricted to the provisions of benefits under the Plan), subject only to the claims of the participants' rights under the Plan in an amount equal to the fair market value of the deferred account for each participant.

Total plan assets at June 30, 2004 are \$287,171.

NOTE 9: EXPENDITURES OVER BUDGET

P.A. 621 of 1978 Section 18, as amended, provides that a local unit shall not incur expenditures in excess of the amount appropriated. The approved General Fund budget of the City was adopted at the department level. During the year ended June 30, 2004, the City incurred expenditures in certain departments, which were in excess of the amount budgeted as follows:

	FINAL BUDGET	ACTUAL	UNFAVORABLE VARIANCE
General Fund			
Public Works	\$ 85,899	\$ 86,760	\$ (861)
Parks	23,147	27,357	(4,210)

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2004

NOTE 10: FUND EQUITIES

Reserved, designated and undesignated fund balances and retained earnings at June 30, 2004 were as follows:

	<u>RESERVED</u>	<u>DESIGNATED</u>
<u>Fund Balance</u>		
General Fund		
Police cars	\$	\$ 13,000
Police training – Act 302	918	
Fire truck		21,100
Parks		<u>911</u>
	<u>\$ 918</u>	<u>\$ 35,011</u>
Special Revenue Funds		
Sweet corn days	\$ 2,652	\$
Summer ball program	1,555	
Swimming pool	<u>4,134</u>	
	<u>\$ 8,341</u>	<u>\$ 0</u>
<u>Net Assets</u>		
Enterprise Funds		
Bond repayment	<u>\$ 196,928</u>	<u>\$</u>

NOTE 11: OPERATING TRANSFERS

Interfund transfers for the current year are as follows:

General Fund Activity

Transfers (out) from:	Transfers in to:	
General Fund	Recreation Fund	\$ (27,945)
General Fund	Equipment Fund	<u>(10,000)</u>
	Total	<u>\$ (37,945)</u>
Recreation Fund	General Fund	\$ 1,000
Major Street Fund	General Fund	6,000
Local Street Fund	General Fund	2,000
Sewer Fund	General Fund	25,000
Water Fund	General Fund	<u>20,000</u>
	Total	<u>\$ 54,000</u>

Recreation Fund Activity

Transfers (out) from:	Transfers in to:	
Recreation Fund	Water Fund	<u>\$ (200)</u>

CITY OF LITCHFIELD, MICHIGAN

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2004

NOTE 11: OPERATING TRANSFERS (CONCLUDED)

Transfers from the General Fund to other funds are to support the operations of those funds. Transfers from other funds to the General Fund are reimbursements for administration support.

Transfers from the Recreation Fund to the Water Fund is reimbursement for water usage in the City's swimming pool.

NOTE 12: RISK MANAGEMENT

The City of Litchfield, Michigan is exposed to various risks of loss related to property loss, torts, errors, and omissions, employee injuries, unemployment benefits, as well as medical and workmen's compensation benefits provided to employees. The City of Litchfield, Michigan has purchased commercial insurance for general liability on buildings and property, equipment damage and theft, employee theft, and limited tort claims for specific City of Litchfield, Michigan facilities or events.

The City participates in the Michigan Municipal League Workers Compensation Fund, a public risk pool established to operate a common risk management and insurance program for municipalities. The City pays premiums to the Fund for its workers' disability compensation insurance coverage. The agreement for formation of the fund provides that the Fund will be self-sustaining through member premiums.

The City continues to carry commercial insurance for all other risks of loss, including employee health and accident insurance. Settled claims for the commercial insurance have not exceeded the amount of coverage in any of the past three years. There was no reduction in coverage obtained through commercial insurance during the past year.

NOTE 13: CONTINGENCIES

Under the terms of various Federal and State grants and regulatory requirements, periodic audits are required and certain costs may be questioned as not being appropriate expenditures under the terms of the grants and requirements. Such audits could lead to reimbursement to the grantor or regulatory agencies. However, City management does not believe such disallowances, if any, will be material to the financial position of the City.

As is the case with other entities, the City faces exposure from potential claims and legal proceedings involving environmental matters. No such claims or proceedings have been asserted as of June 30, 2004.

NOTE 14: IMPLEMENTATION OF NEW ACCOUNTING STANDARDS

For the year ended June 30, 2004 the Authority implemented the following Governmental Accounting Standards Board pronouncements:

Statements

No. 33 – *Accounting and Financial Reporting for Nonexchange Transactions*

No. 34 – *Basic Financial Statements – and Management's discussion and analysis – for State and Local Governments*

No. 36 – *Recipient Reporting for Certain Shared Nonexchange Revenues – An Amendment to GASB No. 33*

No. 37 – *Basic Financial Statements – and Management's discussion and analysis – for State and Local Governments: Omnibus*

No. 38 – *Certain Financial Statement Note Disclosures*

Interpretations

No. 6 – *Recognition and Measurement of certain Liabilities and Expenditures in Governmental Fund Financial Statements*

CITY OF LITCHFIELD, MICHIGAN  
NOTES TO FINANCIAL STATEMENTS (CONCLUDED)  
JUNE 30, 2004

NOTE 14: IMPLEMENTATION OF NEW ACCOUNTING STANDARDS (CONCLUDED)

The above pronouncements are all related to the new financial reporting requirements for all state and local governments. These pronouncements are scheduled for a phased implementation (based on the size of the government) through fiscal years ending prior to June 15, 2005. The City is required to implement the new requirements no later than the fiscal year ending June 30, 2004.

As a result of implementing these pronouncements for the year ended June 30, 2004, the following restatements were made to beginning fund balance and net asset accounts:

Fund Balance – Governmental Activities – June 30, 2003	\$ 488,774
Prior period restatement:	
Accrue payroll liability at June 30, 2003 to comply with GASB No. 34 accrual requirements	<u>(14,625)</u>
Fund Balance – Restated	\$ 474,149
Additions:	
Governmental capital assets, including land, buildings and equipment as of July 1, 2003	1,529,427
Receivables expected to be collected in future years	1,145
Investment in joint venture	13,066
Subtractions:	
Accumulated depreciation as of July 1, 2003 on the above capital assets	323,383
Long-term liabilities to be paid in future years	110,747
Fund balance transferred to create a new Internal Service Fund	<u>7,746</u>
Governmental net assets, restated at July 1, 2003	<u>\$ 1,575,911</u>

REQUIRED SUPPLEMENTAL INFORMATION

CITY OF LITCHFIELD, MICHIGAN  
REQUIRED SUPPLEMENTAL INFORMATION  
BUDGETARY COMPARISON SCHEDULE  
GENERAL FUND  
YEAR ENDED JUNE 30, 2004

	ORIGINAL BUDGET	FINAL AMENDED BUDGET	ACTUAL	FINAL TO ACTUAL
REVENUE				
Taxes	\$ 353,632	\$ 353,632	\$ 356,880	\$ 3,248
Federal revenues			883	883
State revenues	153,376	145,385	148,112	2,727
Charges for services	50,656	69,410	47,351	(22,059)
Licenses and permits	10,040	8,340	9,008	668
Fines, fees, and forfeits	5,900	5,900	6,026	126
Component unit contributions	22,000	51,225	50,875	(350)
Interest	8,000	8,000	9,375	1,375
Lease revenue	5,385	5,385	5,385	-
Other	2,400	12,245	12,505	260
TOTAL REVENUES	<u>\$ 611,389</u>	<u>\$ 659,522</u>	<u>\$ 646,400</u>	<u>\$ (13,122)</u>
EXPENDITURES				
General government	\$ 327,541	\$ 327,114	\$ 292,824	\$ 34,290
Police	278,858	275,608	260,606	15,002
Public works	69,957	85,899	86,760	(861)
Parks	19,193	23,147	27,357	(4,210)
Debt service:				
Principal	23,023	30,573	30,572	1
Interest	3,133	3,513	3,513	
Capital outlay	8,670	8,670	24,421	(15,751)
TOTAL EXPENDITURES	<u>\$ 730,375</u>	<u>\$ 754,524</u>	<u>\$ 726,053</u>	<u>\$ 28,471</u>
REVENUES OVER (UNDER) EXPENDITURES	<u>\$ (118,986)</u>	<u>\$ (95,002)</u>	<u>\$ (79,653)</u>	<u>\$ 15,349</u>
OTHER FINANCIAL SOURCES (USES)				
Operating transfers in	\$ 53,000	\$ 53,000	\$ 54,000	\$ 1,000
Operating transfers (out)	(11,955)	(2,670)	(37,945)	(35,275)
TOTAL OTHER FINANCING SOURCES (USES)	<u>\$ 41,045</u>	<u>\$ 50,330</u>	<u>\$ 16,055</u>	<u>\$ (34,275)</u>
REVENUES AND OTHER SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING (USES)	<u>\$ (77,941)</u>	<u>\$ (44,672)</u>	<u>\$ (63,598)</u>	<u>\$ (18,926)</u>
FUND BALANCE - BEGINNING OF YEAR	<u>306,980</u>	<u>306,980</u>	<u>306,980</u>	
FUND BALANCE - END OF YEAR	<u><u>\$ 229,039</u></u>	<u><u>\$ 262,308</u></u>	<u><u>\$ 243,382</u></u>	<u><u>\$ (18,926)</u></u>

See accompanying notes to the basic financial statements.

CITY OF LITCHFIELD, MICHIGAN  
REQUIRED SUPPLEMENTAL INFORMATION  
BUDGETARY COMPARISON SCHEDULE -  
MAJOR SPECIAL REVENUE FUND -  
MAJOR STREET

YEAR ENDED JUNE 30, 2004

	ORIGINAL BUDGET	FINAL AMENDED BUDGET	ACTUAL	FINAL TO ACTUAL
REVENUE				
State revenues	\$ 97,979	\$ 85,291	\$ 95,091	\$ 9,800
Interest	700	700	1,762	1,062
TOTAL REVENUES	<u>\$ 98,679</u>	<u>\$ 85,991</u>	<u>\$ 96,853</u>	<u>\$ 10,862</u>
EXPENDITURES				
Trunkline maintenance	\$ 11,220	\$ 7,955	\$ 4,280	\$ 3,675
Bridge maintenance		1,224	1,224	
Road maintenance	38,397	32,708	27,900	4,808
Operating supplies	16,600	1,600	2,328	(728)
Employee benefits	9,477	9,477	5,969	3,508
TOTAL EXPENDITURES	<u>\$ 75,694</u>	<u>\$ 52,964</u>	<u>\$ 41,701</u>	<u>\$ 11,263</u>
REVENUES OVER EXPENDITURES	<u>\$ 22,985</u>	<u>\$ 33,027</u>	<u>\$ 55,152</u>	<u>\$ 22,125</u>
OTHER FINANCING SOURCES (USES)				
Operating transfers in	\$	\$	\$	\$
Operating transfers (out)	(6,000)	(6,000)	(6,000)	
TOTAL OTHER FINANCING (USES)	<u>\$ (6,000)</u>	<u>\$ (6,000)</u>	<u>\$ (6,000)</u>	<u>\$</u>
REVENUES AND OTHER SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING (USES)	<u>\$ 16,985</u>	<u>\$ 27,027</u>	<u>\$ 49,152</u>	<u>\$ 22,125</u>
FUND BALANCE - BEGINNING OF YEAR	<u>108,354</u>	<u>108,354</u>	<u>108,354</u>	
FUND BALANCE - END OF YEAR	<u><u>\$ 125,339</u></u>	<u><u>\$ 135,381</u></u>	<u><u>\$ 157,506</u></u>	<u><u>\$ 22,125</u></u>

See accompanying notes to the basic financial statements.

OTHER REPORTS



Osbourne, March, Condon & Co., P.C.

Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON  
INTERNAL CONTROL OVER FINANCIAL REPORTING BASED  
ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN  
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the City Council  
City of Litchfield  
Litchfield, Michigan

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of City of Litchfield as of and for the year ended June 30, 2004, which collectively comprise the City of Litchfield's basic financial statements and have issued our report thereon dated August 27, 2004. We did not audit the financial statements of the Litchfield Fire Department, a joint venture between the City of Litchfield and Litchfield Township, which the financial statements reflect the City's total share of assets and revenues constituting one percent of the related consolidated totals. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Litchfield Fire Department, a joint venture between the City of Litchfield and Litchfield Township, is based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the City of Litchfield's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City of Litchfield's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weakness. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted matters involving the internal control over financial reporting that we have reported to management of City of Litchfield, Michigan, in a separate letter dated August 27, 2004.

This report is intended for the information of the City Council, management and the State of Michigan. However, this report is a matter of public records and its distribution is not limited.

*Osbourne, March, Condon + Co., P.C.*

Certified Public Accountants

Hillsdale, Michigan  
August 27, 2004



Osbourne, March, Condon & Co., P.C.

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August 27, 2004

To the City Council  
City of Litchfield  
Litchfield, Michigan 49252

We have audited the financial statements of City of Litchfield for the year ended June 30, 2004, and have issued our report thereon dated August 27, 2004. Professional standards require that we provide you with the following information related to our audit.

1. Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by City of Litchfield are described in Note 1 to the financial statements. We noted no transactions entered into by City of Litchfield during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

2. Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of the significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. Budget information is the only estimate noted during our audit.

3. Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on City of Litchfield's financial reporting process (that is, cause future financial statements to be materially misstated). In our judgment, none of the adjustments we proposed, whether recorded or unrecorded by the City of Litchfield, either individually or in the aggregate, indicate matters that could have a significant effect on the City of Litchfield's financial reporting process.

4. Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

5. Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the City of Litchfield's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

6. Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City of Litchfield auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

7. Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing our audit.

This information is intended solely for the use of the City of Litchfield. It is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

*Astourne, March, Condon + co., P.C.*

Certified Public Accountants



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August 27, 2004

City Council  
City of Litchfield  
Litchfield, Michigan

In planning and performing our audit of the financial statements of the City of Litchfield for the year ended June 30, 2004, we considered the City of Litchfield's internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

However, during our audit, we became aware of a matter that is an opportunity for strengthening internal control and operating efficiency. The memorandum that accompanies this letter summarizes our comment and suggestion regarding this matter. This letter does not affect our report dated August 27, 2004, on the financial statements of the City of Litchfield.

We will review the status of these comments during our next audit engagement. We have already discussed these comments and suggestions with the City Manager, and we will be pleased to discuss it in further detail at your convenience, to perform any additional study of this matter, or to assist you in implementing the recommendation.

*Osbourne, March, Condon & Co., P.C.,*

Certified Public Accountants

## **CERTIFICATES OF DEPOSIT**

At June 30, 2004 the City has eighteen certificates of deposits with fifteen different financial institutions. Based on our inquiry of City Treasurer, Jill Adams, Council instructed her to spread the money to mitigate its risk of maintaining uninsured bank deposits. This appears to be an excessive spread of deposits in light of the risks of maintaining uninsured bank deposits. There does not appear to be a cost benefit in administering these numerous deposits in light of the risks of losing the deposits due to a financial institution bankruptcy or other economic factors.

### **Recommendation**

We recommend that Council review its risks of maintaining uninsured deposits, in light of economic factors, cost of administering the deposits, and the cost of foregoing higher interest rates. Based on the outcome of your risk evaluation, make changes in the number of certificates of deposit the City has on deposit with financial institutions, if determined necessary.

## **COMPENSATED ABSENCES**

During our audit we identified several issues surrounding compensated absences. Following are the issues identified:

1. We discovered that the City's compensated absences policy does not address hourly employee's eligibility to participate in comp time benefit. Furthermore, we inquired of City management what positions are defined as hourly vs. salary, and no one was able to direct us to a definition in City Policies nor provide us with a rhetorical answer.
2. Additionally, we discovered that City policy does not address the maximum amount of comp time hours that an employee can accumulate.
3. Furthermore, there appears to be an inequality between salary and hourly positions in that hourly employees are paid overtime pay based on their current rate of pay where as salary employees who accumulate comp time hours could potentially be paid for their accumulated comp time at a higher future rate of pay.

### **Recommendations**

1. City positions are defined as hourly or salary in accordance with Federal and State statutes. Additionally, we recommend that City Council revise its comp time policy to address whether or not hourly employees are eligible to participate in comp time benefits. The City should consult its attorney regarding these matters.
2. City should establish a limitation on the maximum amount of comp time hours that employees can accumulate and revise its policies to include the limitation.
3. City should consult its attorney on legal issues, if any, with the established policy as it relates to the question of inequality between hourly and salary overtime pay.

## **REIMBURSEMENT TO EMPLOYEES FOR WORK RELATED EXPENSES**

Currently the City does not have an established policy addressing reimbursements to employees for work related expenses. This was noted when we identified in various cases that employees did not provide the City's administration office with proper supporting documentation for payment.

### Recommendation

We recommend the City draft a policy that outlines requirements for reimbursement to employees for work related expenses and adopt by resolution. The policy should describe the nature of expenses that will be reimbursed to employees by the City and a description of the types of supporting documentation that should be attached to the request for reimbursement.

### INVENTORY

At year ended June 30, 2004 the City's Water Fund had on hand a variety of unused supplies and parts for repairs of water main breaks. These supplies were expensed in previous years but were not used. In Enterprise Funds, water and sewer funds, unused repair supplies and parts are required to be carried on the books as inventory. When the parts are used inventory is reduced and expense is increased for the repairs made.

We communicated to Superintendent, Dan Wooden, that those supplies and parts should be reported as inventory until such time they are used in a repair. Dan agreed that he would determine the value and quantity of items on hand and create an inventory system to maintain unused supplies and parts. At year end a purchase was made in the amount of \$7,427 for supplies and parts. These items are reported on the Water Fund's balance sheet as inventory on hand.

### ANTIFRAUD PROGRAMS AND CONTROLS

City management, not the auditor, is responsible for designing and implementing effective systems and procedures for preventing, deterring, *and* detecting fraud. Currently the City has a variety of controls in place that mitigate such activity. However, we recommend, the City establish a process for assessing its risk for fraudulent activity and reevaluating those risks on a continuous basis. Furthermore, the City should establish antifraud policies required to be adhered to by all employees. Internal controls and employee programs should be implemented in response to identified risks to mitigate fraudulent activities from occurring.

### CITY POOL

During our audit we made inquiries of a City employee who works in the pool area. She disclosed to us that at times pool employees let people in to use the pool free of charge. We communicated this finding to the City Manager and recommended that he consider setting a tone with the pool employees that such practices are unacceptable.